No. 5661

In the United States Circuit Court of Appeals for the Ninth Circuit

PORTLAND CREMATION ASSOCIATION, A CORPORATION, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

UPON PETITIONS TO REVIEW ORDERS OF THE UNITED STATES BOARD OF TAX APPEALS

BRIEF FOR THE RESPONDENT

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PREVIOUS OPINION

The only previous opinion in the present case is that of the United States Board of Tax Appeals (R. 72), which is reported in 10 B. T. A. 65.

JURISDICTION

The petitions for review in the above-entitled cause involve income taxes for the years 1919, 1920, 1921, and 1922, in the amounts of $5,764.69 for the year 1919, $4,402.68 for the year 1920, $4,519.65 for the year 1921, and $2,192.25 for the year 1922, and are taken from three orders of redetermination by

the United States Board of Tax Appeals, promulgated April 19, 1928, as to the years 1919 and 1922, and April 20, 1928, as to the years 1920 and 1921. (R. 77–80.) The jurisdiction of this court is invoked by petition for review filed October 18, 1928 (R. 2) pursuant to the Revenue Act of 1926, ch. 27. Sections 1001, 1002, 1003, 44 Stat. 9, 110.

QUESTION PRESENTED

Is the petitioner entitled to exclude from gross income for the years 1919, 1920, 1921, and 1922, on the ground that they were trust funds, certain amounts set aside by it for the perpetual care of niches, urns, and vaults?

STATUTES INVOLVED

The pertinent provisions of the Revenue Act of 1918, ch. 18, 40 Stat. 1057, and of the Revenue Act of 1921, ch. 136, 42 Stat. 227, are identical.

The following statutes are from the Revenue Act of 1918:

> SEC. 233. (a) That in the case of a corporation subject to the tax imposed by section 230 the term "gross income" means the gross income as defined in section 213, * * *;
>
> SEC. 213. That for the purposes of this title (except as otherwise provided in section 233) the term "gross income"—
>
> (a) Includes gains, profits, and income derived from salaries, wages, or compensation for personal service (including in the case of the President of the United States, the judges of the Supreme and inferior courts

> of the United States, and all other officers and employees, whether elected or appointed, of the United States, Alaska, Hawaii, or any political subdivision thereof, or the District of Columbia, the compensation received as such), of whatever kind and in whatever form paid, or from professions, vocations, trades, businesses, commerce, or sales, or dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from interest, rent, dividends, securities, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever. * * *.

STATEMENT OF FACTS

The petitioner was organized under the laws of the State of Oregon, for the purpose of constructing, maintaining, and operating crematories and columbaria and conducting the business of incinerating human remains and the burial and perpetual care of the ashes resulting therefrom, and conducting the business of funeral director and undertaker. During the years in question the petitioner operated a crematorium and sold niches and vaults in a building maintained for the repository of incinerated human remains and for the burial of the dead. (R. 67.) Deeds, identical in form save as to the description of the particular niche or vault, were given to purchasers. These deeds contained a covenant, running to the grantee and his heirs, that the petitioner would maintain the columbarium

containing the niche or vault forever. (R. 68.) At a meeting of the Board of Directors, on March 3, 1920, a resolution was adopted setting aside, from and after January 1, 1919, twenty per cent of the gross receipts from the sale of niches, urns, and vaults, to the maintenance fund. (R. 69.) During the years in question, the following amounts, equal to twenty per cent of the gross sales price of all urns, niches, and vaults sold by it were placed in the permanent maintenance fund: For the year 1919, $12,827.16; 1920, $17,906.20; 1921, $17,076.73; 1922, $17,538.03. During 1919 this amount was set aside by an informal agreement of the Acting Board of Directors, which action was confirmed by the Directors' meeting mentioned above, and by a stockholders' meeting of December 11, 1919. (R. 70, 68.) For the years 1920, 1921, and 1922, the additions to the maintenance fund were made pursuant to the above-mentioned resolution.

All sales by the petitioner were made with the representation to the purchasers that the covenant to maintain the property was backed by a permanent maintenance fund, and that a portion of the purchase price would be placed in that fund, which fund could not be used for any other purpose. No representations were made as to the handling and control of the fund, save that it was to be handled and controlled by the petitioner. The income from the maintenance fund has at all times been used for the maintenance and upkeep of the property sold, but always through the regular income and expense

accounts of the corporation. The income from the fund was mingled with other income and expended for maintenance along with other funds of the petitioner, and was credited during the years in question directly to the profit and loss account. (R. 70–71.)

During the years in question the maintenance and upkeep of the property required more money than the income from the maintenance fund. This deficiency was supplied from the income of petitioner, and not from the principal of the maintenance fund. Prior to November 3, 1920, there was no separate investment account maintained for this fund, but the amounts thereof were in part mingled with other assets of the petitioner. On that date the petitioner invested $29,816.51 in Liberty Bonds, and these were carried in an account entitled "Investment-Reserve for Maintenance." (R. 71.) Additions were made to this account during 1921, the balance in the account on December 31, 1921, being $35,548.09. On December 31, 1922, the balance to the credit of this account was $65,348.12, included in which was a loan of $20,000 made by the fund to the petitioner. The petitioner's books of account showed as gross sales the amounts received from the purchase of urns, niches, and vaults, less twenty per cent thereof, which was placed in the maintenance fund, and which did not appear as a part of the item "gross sales." (R. 72.) The Commissioner of Internal Revenue determined deficiencies

for the years in question, and from his determinations the petitioner appealed to the Board of Tax Appeals. (R. 7, 22, 31.) The separate petitions were consolidated for hearing, and thereafter the determinations of the Commissioner were approved by the Board. From the decision of the Board the petitioner brings this petition for review.

SUMMARY OF ARGUMENT

No trust was created either orally or in writing and none can be implied from the circumstances of this case. The decision of the Board of Tax Appeals was right on the facts and the same should be affirmed.

ARGUMENT

The amounts received by petitioner from the sale of niches and vaults, and placed in a permanent maintenance fund, do not constitute a trust and must be considered in determining the petitioner's gross income

The only question for determination in this case is whether or not the amounts set aside by the petitioner for the maintenance fund constitute a trust of which petitioner is the trustee, and the niche or vault owners are the beneficiaries. If the maintenance fund was a trust fund, then it is conceded that the sums in question can not be considered in computing the gross income of petitioner. If it was not a trust fund, however, then these sums must be so considered, and the Board of Tax Appeals must be sustained.

Examination shows that the facts are not such as would lead a court to impress the fund with a trust.

Each deed given by petitioner for a vault or niche contained a covenant to the effect that the property would be perpetually maintained. Such a covenant amounts to no more than a contractual obligation. Salesmen of petitioner represented to prospective purchasers that a proportion of the purchase price would be devoted to this fund, but it does not appear that any representations were made as to the proportion of the purchase price to be so devoted. An allocation to the fund of one per cent, rather than twenty per cent, would be a compliance with such representations as were made. Giving to such representations their maximum effect, it can not be said that they do more than create a contract obligation. It thus appears that the contracts with purchasers do not create a trust, either written or oral, express or implied.

Other facts developed by the record directly tend to negative the idea of a trust, and show that the fund was no more than a reserve set aside to take care of future expenses. Such a reserve is not deductible from gross income. In this connection it may be noted that the fund is designated by petitioner as "Investment-Reserve for Maintenance (Liberty Bonds, W. S. S., etc.)." (R. 71.)

Prior to January 1, 1919, the amount placed in this maintenance fund was ten per cent of the gross purchase price, rather than twenty per cent as was the case after that date. It should be noted also that for the year 1919 the amount was set aside by acting officers and their action was not ratified

until a year later, when it might have been completely disaffirmed. It is inconsistent with the idea of a valid trust that the officers *of the trustee* possessed the power to dissipate the fund or divert it to alien purposes. There was no obligation on the part of the petitioner to set aside any particular portion of the purchase price, the amount set aside was not known to the prospective purchaser, and there was no obligation on the company to maintain in the fund such sums or proportions as were credited to it. Moreover, the facts point to the conclusion that the fund was not considered by petitioner as a trust fund. It, with its income, was freely mingled with other funds of the company up to the year 1922, and was considered so much the property of petitioner that it felt itself at liberty to borrow from the fund for its own use.

The petitioner in the instant case is seeking to exclude from gross income twenty per cent of the gross amounts received from the sale of niches and vaults for the purpose of maintenance, yet the petitioner has been allowed as a deduction from gross income the amounts actually expended or incurred during the taxable years for such maintenance. The record does not directly disclose this to be true, but it is disclosed in an indirect way. The Board in its opinion states as follows (R. 73):

> Of course such sum as it expends or incurs annually in the performance of its business functions, whether of maintenance or otherwise, is a proper deduction.

The Board then states that judgment will be entered on fifteen days' notice. (R. 74.) Thereafter the Board entered its judgments in accordance with the judgments proposed by the Commissioner pursuant to the Board's report of January 20, 1928. Notice of the proposed judgments was given to petitioner and petitioner did not oppose. (R. 78, 79, 80.) The judgments entered by the Board found the same deficiencies that the Commissioner had proposed in the three deficiency notices. (R. 13, 26, 35.)

It is thus clear and can not be disputed that the Commissioner in his determination of the deficiencies included in gross income the full amounts received from the purchasers of the niches and vaults and allowed as a deduction for expenses the amounts actually expended or incurred in the maintenance of the niches and vaults. The petitioner accordingly has not been deprived of a deduction from gross income of the amounts actually expended or incurred during the taxable years in the performance of its obligation to maintain the niches and vaults.

There has been one decision by a Federal district court upon a question similar to the one here involved and six decisions by the Board of Tax Appeals. The holdings in these cases are all consistent with the position taken by the Commissioner in this case.

In the case of *Troost Avenue Cemetery Co.* v. *United States*, 21 F. (2d) 194, the association exe-

cuted a trust agreement with a trust company whereby the company received and held a certain percentage of the gross amount received from the sale of cemetery lots in trust for the benefit of the then owners and for the purchasers of said lots absolutely free of any control on the part of the Cemetery Association. The court there held that a trust had been created and that the amounts devoted to this trust could not be considered as a part of the gross income of the Cemetery Association. Comparison of that with the instant case will clearly demonstrate the essential differences which make impossible a like conclusion. The instant case shows no such clear segregation of the funds set aside for maintenance nor does it show any such definite agreement as to the allocation of a specific part of the purchase price.

The decisions of the Board of Tax Appeals, wherein it was held that a trust fund had been established, reveal similarly important distinctions.

In the *Appeal of the Los Angeles Cemetery Association,* 2 B. T. A. 495, the Board held that a trust was created. A separate and specific sum was paid for perpetual care *in addition to the sum paid as the purchase price of the grave or plot.* The agreement providing for the payment of the separate and specific sum was in writing. In the instant case there was no oral or written agreement whereby a separate and specific sum was paid to be used for perpetual care. The Board in that case based its decision primarily upon the provisions of the Cali-

fornia Civil Code, Section 617, which provides tha the sums received by virtue of a contract for perpetual care can only be used for such purposes and prescribes the securities in which the perpetual care funds may be invested. The statutes of Oregon contain no such provisions.

In the *Appeal of Greenwood Cemetery Association,* 2 B. T. A. 910, the Board held that a trust was established upon the authority of the *Appeal of the Los Angeles Cemetery Association, supra.* In the *Greenwood case* the association had published rules and regulations of the cemetery in full as well as the plans for the perpetual care and the charges therefor. The lot prices and the charge for perpetual care were quoted separately to prospective purchasers and when sales were made the charges for the lot and for perpetual care were separate items. According to the agreement the principal paid in for perpetual care is held as a trust fund. The agreement for perpetual care was a written agreement.

The distinction between the *Greenwood case* and the instant case is obvious. In that case there was a written agreement providing that the principal paid in for perpetual care was to be held as a trust fund. There are other differences, but since there was an express declaration of trust in that case such differences need not be pointed out.

In the case of *The Metairie Cemetery Association* v. *Commissioner of Internal Revenue*, 4 B. T. A. 903 the Board held that a trust had been created.

In that case the Board in its opinion stated as follows (p. 909–910):

> There is no conflict in the evidence here with respect to the contracts. The evidence is that at the time the contracts were entered into it was agreed that the money would be held in trust for the specific purposes of the contract. This being true, we are of the opinion that a valid trust was created by parole in those contracts where there was no specific provision to that effect. The only reason that certain of the contracts contained that express provision was the fact that those lot owners insisted upon the agreement being included in writing in the contract. The same agreement, however, was actually made with all of the lot owners verbally.

This language of the Board makes clear the distinction between the *Metairie case* and the instant case. In that case there were express agreements, some oral and some in writing, that the money for perpetual care would be held in trust.

It is conceded that such a trust may be created by oral agreement as the Board held in the *Metairie case,* but in the instant case there was no express agreement either oral or written that a certain portion of the moneys received was to be held in trust.

In the *Appeal of Troost Avenue Cemetery Association,* 4 B. T. A. 1169, the Board held that a trust was established. The facts here were similar to those in *Troost Avenue Cemetery Co.* v. *United States, supra.*

In the case of *Inglewood Park Cemetery Association* v. *Commissioner of Internal Revenue,* 6 B. T. A. 386, the Board held that a trust was created. In that case prospective purchasers were told that twenty-five per cent of the purchase price would go into a fund for the perpetual care of the lots, while in the instant case prospective purchasers were told that a portion, not a *fixed* portion, would be placed in a maintenance fund.

In the *Inglewood case* twenty-five per cent of the purchase price was deposited in a special bank account, while in the instant case prior to November 3, 1920, there was no separate investment account on petitioner's books (R. 44), much less in a special bank account. At no time during the taxable years in the instant case was there maintained a special bank account.

In the *Inglewood case* the Association was governed by the laws of California and the Board based its decision in part upon the provisions of the California Civil Code, Section 617.

Of all the decisions involving perpetual care funds of cemetery associations, there have only been two holding that the moneys received for perpetual care did not constitute a trust fund. These two decisions are the decision of the Board in the instant case and the decision of the Board in the *Appeal of the Springdale Cemetery Association,* 3 B. T. A. 223. In the latter case the certificate of purchase provided for the care of lots during the existence of the cemetery. The taxpayer in that case volun-

tarily set up a reserve for maintenance. That is what happened in the instant case. The opinion in the *Springdale case* does not disclose that there was any express agreement either oral or written as to the establishment of a trust, and that is true in the instant case. The facts in the instant case are much like those in the *Springdale case* and that decision should be regarded as more persuasive here than any other decision of the Board of Tax Appeals.

CONCLUSION

Since there was in the instant case no express agreement, either oral or written, creating a trust, and since a trust cannot be implied from the surrounding circumstances, it is respectfully submitted that the judgment of the Board of Tax Appeals should be affirmed.

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